An Overview of UK Retail Financial Scandals in recent decades: Uses and abuses of Behavioral Finance.

Abstract

Instances of banks and other financial services companies taking advantage of the cognitive limitations and biases of their retail customers have been numerous and sometimes extremely significant in recent decades. For example, some of the major scandals, which have each resulted in billions of pounds of compensation to customers, have involved the mis-selling of personal pensions, with profit-endowments and PPI policies and there have been numerous other instances of consumer protection issues.

Some scandals have resulted in regulatory action such as the regulators setting specified rates of return to use in investment projections. However, specific concerns are still been raised by regulators (e.g. the FCA), charities and consumer bodies in the UK that factors relating to suboptimal behaviour by consumers relating to issues such as consumer inertia, unfair cross-subsidies, add-on goods and product complexity may lead to poor financial outcomes for those consumers.

This paper gives an overview of the nature of these events with a particular emphasis on the behavioral issues involved. It considers the extent to which institutions can and have exploited their customers, whether customers can be educated or ‘nudged’ into different behaviors and the role of the regulators in preventing future problems.